

# Setting up your Business in Romania

## Issues to consider



Romania, one of the fastest growing European economies (during 2015 it has recorded a GDP increase by 3.8%) has taken advantage of the downturn period to implement a series of structural reforms which have already created stability and kept the country attractive to foreign investors. Farming, heavy industry, green energy, infrastructure or IT have a huge potential of development due to natural and human resources as well as due to the large local market consisting of a population of 20 million.

However there are a number of issues which you must consider when you are looking to set up your business in Romania. This document takes you through some of the common questions we come across and gives you practical information about the issues you need to consider.

### **What type of Business Structure should we use?**

There are advantages and disadvantages to all of them, and there is no one correct answer, it's all dependent on your specific business circumstances and needs. A brief overview of the main structures is below:

#### **Establishment (a branch of your overseas business)**

- Not a separate legal entity but an extension of the overseas parent company
- No limited liability or ring-fencing of the Romanian operations
- If have a permanent establishment in Romania then profits from this PE are liable to Romanian Corporation tax
- Must file **parent company accounts** to the Romanian tax authorities, as well as PE accounts according to the Romanian accounting standards. The financial period may be different than the calendar year in order to comply to that of the parent company

#### **Limited Company:**

- Provides limited liability and ring-fencing to Romanian operations
- Gives a perception of a local business, with longevity
- Corporation tax to be paid on company profits
- Must file balance sheets to the tax authorities and the reports are transparent
- Accounts require auditing if 2 of the following 3 criteria are met for 2 years in a row: Revenues > EUR 7.3m p/a, Gross Assets > EUR 3.65m p/a, number of employees > 50.

#### **Freelance (individual or partnership):**

- Profits are allocated to members who then pay Income Tax on these profits personally
- The tax residence of the member, and where the profits in the LLP originated will determine in what jurisdiction and how these profits are taxed
- The income may be subject to social charges

# Setting up your Business in Romania

## Issues to consider



### How much Corporation Tax will the business pay?

Current Corporation Tax rate in Romania is 16% (flat).

Small size companies (Revenues < EUR 100,000 p/a and income from consultancy and management of maximum 20% of turnover ("micro-enterprises") turnover tax is compulsory instead of Corporation tax.

Depending on the number of employees, micro-enterprises tax rates are:

- 3% for companies with no employees.
- 2% for companies that have one employee.
- 1% for companies that have at least 2 employees

No modifications of the tax rates are expected.

More Romanian branches of the same foreign company calculate consolidated taxable profit.

Corporate tax return is filed yearly but quarterly prepayments are due.

Fiscal loss can be carried forward 7 years.

Accelerated fiscal depreciation is allowed for all equipment.

### What if we use Romania to set up our holding company?

Romania's tax legislation means that it is a very attractive place to set up a holding company.

Romania has treaties for avoiding the double taxation with more than 80 countries.

EU regulations regarding the taxation of dividends, royalties and interest are fully applicable.

Dividends received from a Romanian company and dividends received by Romanian companies from EU subsidiaries are not taxable.

No withholding tax on dividends is applicable for dividends paid to other EU companies holding at least 10% of the share capital of the company in which a participation is held, for an uninterrupted period of 1 year.

Professional services are less expensive than in other EU countries.

### What if we make cross-border transactions between group companies?

Romania follows internationally recognized **Transfer Pricing** (TP) rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm's length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods

# Setting up your Business in Romania

## Issues to consider



- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc.
- Provision of financial support e.g. inter-group loans and charging a “market” interest on loans

A business will need to prepare a Transfer Pricing Report proving the arm’s length basis of transactions. The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm’s length basis.

Starting January 2016, large taxpayers which carry out transactions with related parties over certain significance thresholds are required to prepare the transfer pricing documentation files on an annual basis. The deadline for TP file is 25 March of the following year.

For large taxpayers the value of materiality level is:

- 200,000 euros for interest received / paid
- 250,000 euros for transactions involving services received / provided
- 350,000 euros for transactions involving purchases / sales of goods.

Large taxpayers carrying out transactions with related parties below the thresholds mentioned above, and all other taxpayers which carry out transactions with related parties over certain (different, see below) significance thresholds, are required to provide their transfer pricing documentation files to the Romanian tax authorities upon their request.

For small and medium taxpayers, who carry out transactions with affiliated parties the value of materiality level is:

- 50,000 euros for interest received / paid
- 50,000 euros for transactions involving services received / provided
- 1000,000 euros for transactions involving purchases / sales of goods.

### **What Employment Taxes and Social Security will need to be paid?**

If an individual is resident in Romania then he is subject to Romanian tax laws. The main residency criteria are: period of staying, reason of arrival, family relations, dwelling places. Upon arrival for long period in Romania any person should submit a questionnaire regarding all above mentioned criteria. Considering the complexity of the matter we would advise any new entrant to Romania or person who spends time working in Romania to take professional advice to determine whether they are Romanian tax resident.

**Current Personal Income Tax rates in Romania are:**

**Income Tax rate is 16% flat.**

Employers and employees also have to pay Romanian social securities

# Setting up your Business in Romania

## Issues to consider



### Current Social Security rates are:

	Band of income (£)	Rate (%)
Employer	Up to RON 13,405*no of employees	22.75
	Over RON 13,405*no of employees	6.95
Employee	Up to RON 13,405	16.5
	Over RON 13,405	6

NB: (rates are for the tax year to 12/31/2016)

RON 13,405 means 5 average monthly salaries and is subject to review every year

Rate of exchange is app RON 4.5/1 EURO

It is the employers' legal responsibility to pay over employee's tax and social security deductions to the Romanian tax authorities. The payments are due on a monthly basis.

Romania has a Reciprocal Agreement with the EU countries and others whereby when an overseas national of those countries is seconded to the Romania for a defined period of time and continues to pay social security in their home country, then the employer and employee are exempt from paying Romanian social security.

### What is Value Added Tax (VAT) and should the business be registered?

VAT is a "goods and services tax" on supplies made, the standard rate of which is 20% (19% from 1 January 2017). If a business makes taxable supplies in excess of EUR 100,000 during a calendar year then it MUST be registered for VAT.

There are three types of supplies:

- Taxable – must charge VAT on supplies, can reclaim input VAT
- Exempt – cannot charge VAT nor reclaim input VAT
- Outside the scope – not within the Romanian VAT system

The supply of most types of goods and services in Romania would be classed as Taxable supplies.

If a Romanian entity sells goods or provides certain services outside Romania then there is no VAT chargeable on this overseas supply, however on the basis that the supply would be VAT'able if made in the Romania then the entity will be able to reclaim all its input VAT.

Reduced rates are applicable for: supply of houses (under 120 sqm and RON 450,000), school books, magazines, admission to shows, theatres, concerts, museums – 5%; supply of medicines, restaurant and catering services, water and hotel accommodation – 9%.

Example of exempted supplies: financial services, hospitalisation, supply of agricultural land, supply of old buildings, rent of real estate. Some exemptions are limited or optional therefore we recommend taking professional advice regarding the classification of the transactions and

# Setting up your Business in Romania

## Issues to consider



the consequences in case that exemption is applicable

### **Can we provide Share option plans to our staff?**

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

Romania has a number of “approved” share option plans which give tax benefits to employees and employers alike however the object of the plans should be the shares of the Romanian employer.

However this is a very technically complex area and careful planning needs to be undertaken as soon as share option plans are being considered for implementation in Romania.

### **How else can we compensate our employees?**

Romania has a very comprehensive range of compensation and benefit options available for companies to offer their employees, among which the following are not taxable: Private pension insurance limited to 400 Euros/year, health insurance premiums, limited to 400 Euros/year, lunch vouchers of app. EUR 2.5 /day (subject only to income tax but exempted from social securities contributions), income tax exemption for software developers, income tax exemption for persons with severe disabilities.

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